

Teacher background reading excerpted and edited -

From Capstone ©1989 Unit 4 Lesson 4 and the Elementary Economist, Theme Public Goods and Services, Volume 3, No. 3 Directions authored by William B. Walstad

Economics - Most economic decisions in the United States and Canada are made in the marketplace—what is frequently referred to as the private sector. While many goods and services can be provided by the private sector, some are best provided by government. Moreover, some goods and services are provided by the public and the private sectors. Private goods and services are ones that can only be consumed by one individual at a time. Public goods and services are ones that can be consumed jointly at no additional cost. Two concepts that explain which goods and services are best provided by government are non-exclusion and shared consumption. Non-exclusion means that it is difficult to exclude non-payers from receiving the benefit of a good or service. Shared consumption means that the consumption of a good or service by one consumer does not reduce the benefit to other consumers.

Reasoning - The ideas of non-exclusion and shared consumption are at the heart of the economic system. When people can obtain a good or service whether they pay for it or not, they have less incentive to pay. If consumers have not incentive to pay the costs producers will have little incentive to provide the benefits. AS a result, such goods and services will not be produced despite the fact that everyone wants them. This explains why the role of government is so important. Government can provide goods and services when it is difficult to exclude non-payers and when the product or service involves shared consumption. Through taxation, government can require all citizens to pay for their share so no one gets a “free” good or service. For example, everyone desires police protection. However, because it is difficult to exclude people from the benefits of police protection, government supplies the service to everyone, and everyone pays for it through taxation. Markets and government differ in the way people are charged for goods and services. Under the market system, “you get what you pay for.” If you want to buy and use a bicycle, you must pay the seller the agreed price. However, most public goods and services are provided to users without a direct charge. People usually do not pa directly for national defense, road, parks, and elementary and secondary education, but rather they pay indirectly through taxes. Furthermore, the amount of taxes paid may not reflect the quantity of public goods and service consumed by the individual. Even in situations where people are directly charged for public goods or service, such as for postage stamps or park entry permits, the fee are less than the actual cost since government subsidizes many public activities. In addition, market and public decision-making are significantly different; in a market; buyers and sellers make their decisions independently of each other, based on an examination of their respective opportunity costs. Public decision making, however, occurs in city halls, state legislatures, and those places, where elected representatives make decisions which affect a large group of people, not just themselves and as individuals. This type of bargaining and decision-making is complex, involves large amounts of money, and is subject to the balancing of political as well as economic considerations.

While the market price system accounts for the production and distribution of most goods and services in the economy, government performs many valuable functions. The most noteworthy function is the provision of public goods and services. By definition, a public good or service is one that cannot be provided exclusively to those who agree to pay for it. With private goods and services, those who pay receive the benefits, but with public goods and services, there is not an effective way to prevent non-payers from benefiting. In other words, the exclusion principle for the private sector fails to work with certain goods and services, so the government must provide them. In addition public goods and services are usually less dividable than private goods and services, making it difficult to sell separate units to individual consumers.